Nos. 15,011 - 15,015

In the United States Court of Appeals for the Ninth Circuit

UNITED STATES OF AMERICA, Appellant
v.
MONTE L. WOLF, Executor of the Estate of Harry J. Wolf, deceased, Appellee

UNITED STATES OF AMERICA, Appellant
v.
MONTE L. WOLF, Transferee of the Estate of Jennie Wolf, deceased, Appellee

UNITED STATES OF AMERICA, Appellant
v.
BLOSSOM M. GRAYSON, Transferee of the Estate of Jennie Wolf, deceased, Appellee

UNITED STATES OF AMERICA, Appellant
v.
CHARLOTTE C. COHON, Transferee of the Estate of Jennie Wolf, deceased, Appellee

UNITED STATES OF AMERICA, Appellant
v.
MANUEL SCHNITZER, HAROLD SCHNITZER and LEONARD SCHNITZER, Executors of the Estate of Sam Schnitzer, deceased, Appellees

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On Appeal from the Judgments of the United States District Court for the District of Oregon

BRIEF FOR THE APPELLANT

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MISCELLANEOUS

In the United States
Court of Appeals
for the Ninth Circuit

No. 15,011

UNITED STATES OF AMERICA, Appellant
v.
MONTE L. WOLF, Executor of the Estate of Harry J. Wolf, deceased, Appellee

No. 15,012

UNITED STATES OF AMERICA, Appellant
v.
MONTE L. WOLF, Transferee of the Estate of Jennie Wolf, deceased, Appellee

No. 15,013

UNITED STATES OF AMERICA, Appellant
v.
BLOSSOM M. GRAYSON, Transferee of the Estate of Jennie Wolf, deceased, Appellee

No. 15,014

UNITED STATES OF AMERICA, Appellant
v.
CHARLOTTE C. COHON, Transferee of the Estate of Jennie Wolf, deceased, Appellee

No. 15,015

UNITED STATES OF AMERICA, Appellant
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MANUEL SCHNITZER, HAROLD SCHNITZER and LEONARD SCHNITZER, Executors of the Estate of Sam Schnitzer, deceased, Appellees

On Appeal from the Judgments of the United States District Court for the District of Oregon

BRIEF FOR THE APPELLANT

OPINION BELOW

The District Court wrote no opinion.

JURISDICTION

These appeals involve federal income and victory taxes. The taxes for 1942 and 1943 were paid on or before March 15, 1943, and March 15, 1944, respectively:

Docket No.	Taxpayer	Record references
15,011	Monte L. Wolf, Executor	R. 43-44
15,012	Monte L. Wolf, Transferee	R. 42-43
15,013	Blossom M. Grayson, Transferee	R. 5-6
15,014	Charlotte C. Cohon, Transferee	R. 5-6
15,015	Manuel Schnitzer, Harold Schnitzer, and Leonard Schnitzer, Executors	R. 5-6

The Tax Court held that taxpayers were liable for deficiencies for the year 1943. These deficiencies were paid on December 30, 1949:

Docket No.	Taxpayer	Record references
15,011	Monte L. Wolf, Executor	R. 47
15,012	Monte L. Wolf, Transferee	R. 46
15,013	Blossom M. Grayson, Transferee	R. 9
15,014	Charlotte C. Cohon, Transferee	R. 9
15,015	Manuel Schnitzer, Harold Schnitzer, and Leonard Schnitzer, Executors	R. 8-9

Taxpayers then made claims for refunds for the year 1943[1/] on June 21, 1951, and on August 1, 1951, the Commissioner notified them that their claims had been disallowed:

Docket No.	Taxpayer	Record references
15,011	Monte L. Wolf, Executor	R. 48-49
15,012	Monte L. Wolf, Transferee	R. 47-48
15,013	Blossom M. Grayson, Transferee	R. 10-11
15,014	Charlotte C. Cohon, Transferee	R. 10-11
15,015	Manuel Schnitzer, Harold Schnitzer, and Leonard Schnitzer, Executors	R. 10

On July 31, 1953, taxpayers brought these suits pursuant to Section 3772(a) of the Internal Revenue Code of 1939. Jurisdiction is conferred on the District Court by 28 U.S.C., Section 1346. Judgments of recovery for taxpayers were entered on August 19, 1955, as follows:

Docket No.	Taxpayer	Amount	Record references
15,011	Monte L. Wolf, Executor	$41,608.89	R. 71, 76
15,012	Monte L. Wolf, Transferee	13,025.09	R. 65, 69
15,013	Blossom M. Grayson, Transferee	13,025.09	R. 25-26
15,014	Charlotte C. Cohon, Transferee	13,025.09	R. 25-26
15,015	Manuel Schnitzer, Harold Schnitzer, and Leonard Schnitzer, Executors	41,719.77	R. 25

Notices of appeal were filed on October 14, 1955:

[1/] Actually both the years 1942 and 1943 are involved but due to the application of the Current Tax Payment Act of 1943, c. 120, 57 Stat. 126, only the year 1943 is officially in issue.

Docket No.	Taxpayer	Record reference
15,011	Monte L. Wolf, Executor	R. 72
15,012	Monte L. Wolf, Transferee	R. 66
15,013	Blossom M. Grayson, Transferee	R. 26
15,014	Charlotte C. Cohon, Transferee	R. 26
15,015	Manuel Schnitzer, Harold Schnitzer, and Leonard Schnitzer, Executors	R. 26

Jurisdiction is conferred on this Court by 28 U.S.C., Section 1291.

QUESTIONS PRESENTED

1. Whether these suits are precluded by Section 322(c) of the Internal Revenue Code of 1939, since the Commissioner has mailed the taxpayers notice of deficiency and they filed petitions with the Tax Court for the same year involved in these suits.

2. In the alternative whether these suits are barred by the doctrine of *res judicata.*

3. If the taxpayers are entitled to refund, whether the District Court figured the amounts of refund correctly.

STATUTES INVOLVED

Internal Revenue Code of 1939:

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

* * * *

(g) *Capital Losses.*—

(1) *Limitation.*—Losses from sales or exchanges of capital assets shall be allowed only to the extent provided in section 117.

* * * *

(2) *Securities becoming worthless.*—If any securities (as defined in paragraph (3) of this subsection) become worthless during the taxable year and are capital assets, the loss resulting therefrom shall, for the purpose of this chapter, be considered as a loss from the sale or exchange, on the last day of such taxable year, of capital assets.

* * * *

(26 U.S.C. 1952 ed., Sec. 23.)

SEC. 117. CAPITAL GAINS AND LOSSES.

* * * *

(d) [As amended by Sec. 150(c) of the Revenue Act of 1942, c. 619, 56 Stat. 798] *Limitation on Capital Losses.*

(2) *Other taxpayers.*—In the case of a taxpayer, other than a corporation, losses from sales or exchanges of capital assets shall be allowed only to the extent of the gains from such sales or exchanges, plus the net income of the taxpayer of $1,000, whichever is smaller. For purposes of this paragraph, net income

shall be computed without regard to gains or losses from sales or exchanges of capital assets.

* * * *

(26 U.S.C. 1952 ed., Sec. 117.)

SEC. 322. REFUNDS AND CREDITS

* * * *

(c) *Effect of Petition to Tax Court.* If the Commissioner has mailed to the taxpayer a notice of deficiency under section 272(a) and if the taxpayer files a petition with the Tax Court within the time prescribed in such subsection, no credit or refund in respect of the tax for the taxable year in respect of which the Commissioner has determined the deficiency shall be allowed or made and no suit by the taxpayer for the recovery of any part of such tax shall be instituted in any court except—

(1) As to overpayments determined by a decision of the Tax Court which has become final; and

(2) As to any amount collected in excess of an amount computed in accordance with the decision of the Tax Court which has become final; and

(3) As to any amount collected after the period of limitation upon the beginning of distraint or a proceeding in court for collection has expired; but in any such claim for credit or refund or in any such suit for refund the decision of the Tax Court which has become final, as to whether

such period has expired before the notice of deficiency was mailed, shall be conclusive.

(d) [As amended by Sec. 14(d) of the Individual Income Tax Act of 1944, c. 210, 58 Stat. 231] *Overpayment Found by Tax Court.* — If the Tax Court finds that there is no deficiency and further finds that the taxpayer has made an overpayment of tax in respect of the taxable year in respect of which the Commissioner determined the deficiency or finds that there is a deficiency but that the taxpayer has made an overpayment of tax in respect of such taxable year, the Tax Court shall have jurisdiction to determine the amount of such overpayment, and such amount shall, when the decision of the Tax Court has become final, be credited or refunded to the taxpayer. * * *

* * * *

(26 U.S.C. 1952 ed., Sec. 322.)

STATEMENT

During the years 1942 and 1943, and for many years prior thereto, Sam Schnitzer, his wife, Rose Schnitzer, Harry J. Wolf and his wife, Jennie Wolf, operated the Alaska Junk Company of Portland, Oregon, as a copartnership. (R. 42-

43.)[2] During 1942 and 1943, Alaska Junk delivered merchandise to Oregon Electric Steel Rolling Mills, and the amount of these items was carried on the books of Alaska Junk as accounts receivable. (R. 43-44.) Alaska Junk, on its partnership return for 1943, claimed as a bad debt deduction $202,350.60, the balance carried on its books as accounts receivable from Oregon Electric. (R. 44). The Commissioner determined deficiencies on the grounds that Rose Schnitzer and Jennie Wolf were not bona fide partners for tax purposes during the years 1942 and 1943 (Tax Court R. 53),[3] and that the bad debt deduction in 1943 was not allowable. (R. 45). The partners (or their transferees or executors) petitioned the Tax Court for redetermination of their income taxes for the years 1942 and 1943. (Tax Court R. 2-15.) The Tax Court held that Rose Schnitzer and Jennie Wolf were bona fide partners for tax purposes and that Alaska Junk had supplied goods to Oregon Electric at cost, but disallowed the bad debt deduction on the ground that the amounts charged to Oregon Electric Steel Rolling Mills were contributions to capital and not the result of sales.

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[2]/All further record references are to the record in No. 15,011, *United States of America* v. *Monte L. Wolf, Executor*, unless indicated otherwise.

[3]/References to Tax Court record are to the record in the case of *Schnitzer* v. *Commissioner*, Court of Appeals Docket No. 12,471. (Joint Pre-Trial Ex. No. 1.)

Schnitzer v. *Commissioner*, 13 T.C. 43, affirmed *per curiam*, 183 F. 2d 70 (C.A. 9th), certiorari denied, 340 U.S. 911.

The Tax Court withheld entry of its decisions, pursuant to Rule 50 of its Rules of Practice, for the purpose of permitting the parties to submit computations of the proper tax liability. The Commissioner filed his computation and the partners (or their transferees or executors) acquiesced in the computation. The Tax Court thereupon entered its final orders and decisions determining deficiencies on the part of the taxpayers. Upon appeal by the taxpayers this Court affirmed *per curiam*, 183 F. 2d 70, certiorari denied, 340 U.S. 911. (R. 45-46.)

The pre-trial order provides that as a result of the above adjudication, the "sales" to Oregon Electric were erroneously carried on the books of the Alaska Junk Company as accounts receivable. They were erroneously included in the gross income of the partnership for 1942 and 1943. The income and victory taxes paid by the partners on their distributive shares therefrom under the original returns were erroneously paid, and the amounts of such "sales" should have been excluded from the gross income of Alaska Junk Company, thus reducing the amount of the net income reportable by Alaska Junk, and thus reducing the amount of income reportable by the partners on their individual returns. (R. 47-48.) The pre-trial order also provided that the taxpayers did not eliminate the costs of merchandise "sold and delivered" to Oregon,

that is, taxpayers did not reduce the costs of sales reported in the original returns of the partnership by the actual costs of the merchandise "sold and delivered to Oregon." (R. 50.) In the pre-trial order the parties stipulated alternative computations of amounts which the taxpayers would be entitled to recover in the event the court should determine that the prosecution of this action is not barred by Section 322(c) of the 1939 Code, or by the principle of *res judicata,* and/or the doctrine of collateral estoppel. The taxpayers' computation is one derived without reduction of the cost of "sales" as reported in the returns of the partnership by the actual costs of the merchandise delivered to Oregon; and the Government's computation is one which reduces the costs of "sales" as reported in the partnership returns by the actual costs of such merchandise. (R. 50-51.)

The partners (or their executors or transferees) filed claims for refund with the Collector of Internal Revenue for the District of Oregon on June 21, 1951. On August 1, 1951, the claims were disallowed. (See record references under section of brief entitled "Jurisdiction.") These actions followed.

STATEMENT OF POINTS TO BE URGED

1. The District Court erred in holding that taxpayers were not barred from claiming refunds and from bringing

these suits by Section 322(c) of the Internal Revenue Code of 1939.

2. The District Court erred in holding that taxpayers' suits were not barred by the doctrine of *res judicata.*

3. The District Court erred in holding that taxpayers' net profit should be adjusted by deducting the full sales price of goods "sold" to Oregon Electric from Alaska Junk's total gross sales without deducting from the total cost of goods sold the cost of the goods which it held should be eliminated from the gross sales.

SUMMARY OF ARGUMENT

These suits are barred by Section 322(c) of the Internal Revenue Code of 1939 because the Commissioner mailed the taxpayers (or their decedents or transferors) notices of deficiency for the year involved here and the taxpayers filed petitions with the Tax Court for redetermination of the asserted deficiencies. Taxpayers cannot bring themselves within the second exception to Section 322(c) under the broadest interpretation of that exception. Furthermore, the finding of the Tax Court in the previous actions that Alaska Junk supplied Oregon Electric merchandise at cost is diametrically opposed to taxpayers' position here. Taxpayers are seeking to deduct the same item which they tried unsuccessfully to deduct in the previous actions before the Tax Court. These suits are barred by mere reason of the fact that tax-

payers have already petitioned the Tax Court with respect to the tax year involved, and do not depend upon whether taxpayers did or could have raised the issue involved here.

In the alternative, if these suits are not precluded by Section 322(c), they are barred by the doctrine of *res judicata.* The purpose of that doctrine is the saving of judicial time and the establishment of certainty in legal relations. When a court of competent jurisdiction has entered a final judgment on the merits of a cause of action, the parties to the suit and their privies are thereafter bound not only as to every matter which was offered and received to sustain or defeat the claim or demand, but as to any other admissible matter which might have been offered for that purpose. Income tax liability for any one year is a single cause of action. Thus when taxpayers litigated their liability for the year 1943 before the Tax Court, they precluded themselves from relitigating their liability for that year as to any matter which might have been raised in the prior litigation. We submit that the issued raised in the present actions could and should have been presented in the prior suits as an alternative issue to the effect that if the transfers of merchandise to Oregon Electric were held to be contributions to capital and not sales, then the taxes paid on the profit from those "sales" were erroneously paid. Not having raised this issue when they could have, taxpayers should not be permitted to do so now.

Alaska Junk in its returns treated the delivery of merchandise to Oregon Electric as sales. Thus it reported in its net

income only the gains from such "sales," that is, the difference between the "gross sales" price and the cost of the merchandise. It carried the "gross sales" price as accounts receivable and in 1943 deducted the portion it had not been paid as a bad debt. The Commissioner's determination, upheld by the Tax Court, denied the deduction as a bad debt on the ground that the deliveries of this merchandise were capital contributions to Oregon Electric, and not sales. Taxpayers argue that the income they reported from those sales should be reduced by deducting from the total gross sales of Alaska Junk the *"gross sales" price* of merchandise "sold" to Oregon Electric, while leaving the cost of those goods "sold" included in Alaska Junk's total *cost* of goods figure. The Government submits that it is clear that the cost of goods "sold" to Oregon Electric must be deducted from Alaska Junk's total cost of goods sold as well. Since the goods were contributed to the capital of Oregon Electric and not sold, they cannot remain in the cost of goods sold figure. To leave them in that figure while deducting their selling price from the gross sales figure would produce an erroneous net profit figure.

The ruling in the former action is *res judicata* that the partnership suffered no loss upon the merchandise furnished to Oregon; and that any loss therefrom was a capital loss to the individual taxpayers as stockholders of Oregon, deduction of which is limited. Indeed, the Tax Court's finding in the former action that the merchandise was furnished at cost

is *res judicata* and precludes the assertion here of any adjustment of partnership income as returned.

ARGUMENT

I

THESE ACTIONS ARE BARRED BY SECTION 322 (c), OF THE INTERNAL REVENUE CODE OF 1939 BECAUSE THE COMMISSIONER MAILED THE TAXPAYERS NOTICES OF DEFICIENCY, AND TAXPAYERS FILED PETITIONS FOR REDETERMINATION WITH THE TAX COURT. THE AMOUNTS SOUGHT BY TAXPAYERS HERE WERE NOT COLLECTED IN EXCESS OF AMOUNTS COMPUTED IN ACCORDANCE WITH THE DECISIONS OF THE TAX COURT, BUT ARE AMOUNTS COMPUTED IN ACCORDANCE WITH THE DECISIONS OF THE TAX COURT.

Under the Revenue Act of 1924, c. 234, 43 Stat. 253, no direct judicial review of proceedings before the Board of Tax Appeals was provided. However, both the taxpayer and the Government had the right to test the correctness of the Board's action in any court of competent jurisdiction. This procedure was changed in the Revenue Act of 1926, c. 27, 44 Stat. 9, by Section 284(d), which became Section 322(c) of the 1939 Code, *supra,* and a direct judicial review of the Board's decisions by the Courts of Appeals and the Supreme

Court was substituted, and the Board's jurisdiction was enlarged to enable it to consider deficiencies beyond those shown in the Commissioner's notice, and also to determine that the taxpayer not only did not owe the tax but had overpaid it. *Bankers' Reserve Life Co.* v. *United States,* 44 F. 2d 1000, 1003 (C. Cls.), certiorari denied, 283 U.S. 836.

Section 322(c) of the Internal Revenue Code of 1939, *supra,* provides that, if the Commissioner has mailed to the taxpayer a notice of deficiency under Section 272(a) and if the taxpayer files a petition with the Tax Court within the time prescribed in such subsection, no credit or refund in respect of the tax for the taxable year in respect of which the Commissioner has determined the deficiency shall be allowed or made and no suit by the taxpayer for the recovery of any part of such tax shall be instituted in any court, with three exceptions. Thus where a taxpayer petitioned the Board of Tax Appeals to redetermine an asserted deficiency for 1925, and the Board upheld the Commissioner, taxpayer was precluded from paying the deficiency and then bringing a suit for refund of it in District Court. *Cook v. United States,* 108 F. 2d 804 (C.A. 5th), certiorari denied, 310 U.S. 636. Likewise where a taxpayer's petition for redetermination was dismissed by the Tax Court for lack of prosecution, and the Tax Court determined that deficiencies existed as the Commissioner had asserted, the taxpayer was barred from paying the deficiency and suing for refund in the District Court. *Fiorentino* v. *United States,* 226 F. 2d 619 (C.A. 3d).

Furthermore, the Tax Court may determine overpayments (Section 322(d), *supra*), so that where a taxpayer petitions the Tax Court to redetermine an asserted deficiency, and he thinks that he has overpaid, he must show it at that time. Should he fail to do so, he would be barred from any subsequent suit in another court for refund. *Staten Island Shipbuilding Co.* v. *United States,* 31 F. Supp. 166 (C. Cls). This is true even though the ground upon which a refund is sought is entirely distinct from the ground upon which the Commissioner has asserted a deficiency. *Bear Mill Mfg. Co.* v. *United States,* 93 F. Supp. 988 (S.D. N.Y.). These are the general principles with respect to Section 322(c).

The Government believes that the present actions are barred by Section 322(c) in that taxpayers filed petitions in the Tax Court, and hence no credit or refund is now allowable, nor can any suit be instituted. In the court below, taxpayers argued, and the court held, that they could sue by reason of the second exception to Section 322(c) which permits suit for recovery of "any amount collected in excess of an amount computed in accordance with the decision of the Tax Court which has become final." Taxpayers contend that the taxes they paid on the alleged profit from "sales" to Oregon Electric are amounts collected in excess of an amount computed in accordance with the decisions of the Tax Court. We submit, however, that taxpayers cannot bring themselves within exception (2) provided in Section 322(c) under the broadest interpretation of that exception. Taxpayers' position

here is not only not in accordance with the decision in the previous actions, but on the contrary, the findings of the Tax Court in the former suits, which were specifically attacked in this Court upon appeal, and which were affirmed, are diametrically opposed to their position and preclude recovery in the instant suits.

In the former actions, the Tax Court found as a fact (13 T.C. 43, 49) that "From October 1941 Alaska Junk made numerous advances of cash to Oregon Steel, supplied it with goods of various kinds *at cost* * * *." (Italics supplied.) When taxpayers appealed the Tax Court decisions to this Court, they specified that the Tax Court had erred in finding that the goods were supplied at cost (Appellants' Br. 7, 19, *Schnitzer* v. *Commissioner* (Docket Nos. 12,471-12,476)), but this Court affirmed the Tax Court *per curiam,* 183 F 2d 70. Yet taxpayers' claims here are grounded upon the theory that these goods were supplied by Alaska Junk *at a profit.* This is clearly inconsistent with the decisions in the former cases. It is also to be noted that taxpayers assert here that they are entitled to deduct $347,341.62 from the partnership income as returned. This is the exact amount—the same item—which taxpayers asserted in their brief in the former actions (Appellants' Br. 20, *Schnitzer* v. *Commissioner*) in their argument attacking the Tax Court's findings that the goods were furnished at cost.

Further, at the close of the Tax Court proceedings, the Commissioner filed his computation showing taxpayers' total liability, and taxpayers acquiesced therein. (R. 45-46.) It must be assumed that everything which would affect taxpayers' liability was considered, whether raised by the petitions and answers or not. *Lehigh Valley Trust Co.* v. *United States,* 34 F. Supp. 839, 841 (E.D. Pa.). There is then no amount collected in excess of an amount computed in accordance with the decisions of the Tax Court. All the amounts collected are precisely in accordance with the decisions of the Tax Court, and these suits are accordingly barred.

That this is the result intended by Congress is apparent from the report of the Senate Committee on Finance discussing Section 284(d) of the Revenue Act of 1926, c. 27, 44. Stat. 9, predecessor of Section 322(d) of the Internal Revenue Code of 1939, as follows (S. Rep. No. 52, 69th Cong., 1st Sess., pp. 25-26 (1939-1 Cum. Bull. (Part 2) 332, 351)):

> The House bill also provides in section 281(d) that when the deficiency letter has been sent to the taxpayer, whether or not he takes the case to the Board of Tax Appeals, his right to claim or sue for a refund for the year to which the deficiency letter relates is forever barred. This provision seems to the committee too drastic, and it is accordingly proposed in section 284(d) of the bill that the taxpayer's right to claim and sue for refund shall be barred only if he takes the case to the Board, thus preserving to him the option of paying the tax and then proceed-

ing before the Department and the courts to recover any excess payments by a claim or suit for refund.

But if he does elect to file a petition with the Board his entire tax liability for the year in question (except in case of fraud) is finally and completely settled by the decision of the Board when it has become final, whether the decision is by findings of fact and opinion, or by dismissal, as in case of lack of prosecution, insufficiency of evidence to sustain the petition, or on the taxpayer's own motion. The duty of the Commissioner to assess the deficiency thus determined is mandatory, and no matter how meritorious a claim for abatement of the assessment or for refund he cannot entertain it, nor can suit be maintained against the United States or the collector. Finality is the end sought to be attained by these provisions of the bill and the committee is convinced that to allow the reopening of the question of the tax for the year involved either by the taxpayer or by the Commissioner (save in the sole case of fraud) would be highly undesirable.

The Court of Claims has stated also (*Bankers' Reserve Life Co.* v. *United States supra,* p. 1005) that—

Section 284(d) gives effect to the intent of Congress to attain finality to proceedings instituted before the Board of Tax Appeals by barring the right of a taxpayer who takes his case there to bring suit for refund of any part of the taxes paid for the year for which the appeal is taken to the board.

The impossibility of taxpayers' position in the actions at bar does not depend upon whether or not they could have

raised the present issue when they were before the Tax Court. They are barred here simply because they petitioned the Tax Court. *Merrill* v. *United States,* 152 F. 2d 74 (C.A. 2d). This is forcefully shown by the case of *Elbert* v. *Johnson,* 164 F. 2d 421 (C.A. 2d), in which the Commissioner asserted a deficiency against the taxpayer for the year 1938. Taxpayer had also erroneously paid a gift tax in 1938. He petitioned the Tax Court for a redetermination, asking that the erroneously paid gift tax be credited against the alleged deficiency. The Tax Court held that it lacked jurisdiction to allow the mistakenly paid gift tax as a credit. Taxpayer paid the deficiency and then sued in the District Court for refund of the gift tax. The Court of Appeals held that Section 322(c) prevented the suit, saying (p. 424):

> It is not the decision which the Tax Court makes but the fact that the taxpayer has resorted to that court which ends his opportunity to litigate in the District Court his tax liability for the year in question. * * * Hence it is immaterial that the issue sought to be litigated in the District Court was not presented to the Tax Court, or could not have been presented because based on subsequent events.

Again, in *Ross* v. *United States,* 75 F. Supp. 725 (C. Cls.), certiorari denied, 334 U.S. 832, the taxpayer had taken certain deductions for 1935, 1936, and 1937 which the Commissioner disallowed. The taxpayer petitioned the Tax Court which upheld the Commissioner. Subsequently Con-

gress passed a retroactive Act which permitted the deductions the taxpayer had unsuccessfully tried to take. The taxpayer sued for refund in the Court of Claims which held that, even though the statute retroactively allowed the deductions taken by the taxpayer, refund and suit were barred by Section 322(c) merely because the taxpayer had already petitioned the Tax Court for redetermination of the taxes due in the years involved.

In the cases at bar then, taxpayers are precluded merely because they (or their decedents or transferors) have already petitioned the Tax Court; and it makes no difference whether their present claim was presented to or allowed by the Tax Court in those proceedings. Nor do taxpayers qualify under exception two to Section 322(c), for there was no amount collected in excess of an amount computed in accordance with the decisions of the Tax Court which have become final.

II

IN THE ALTERNATIVE, THESE SUITS ARE BARRED BY THE DOCTRINE OF *RES JUDICATA*

The bar to these actions created by Section 322(c) rests solely on the language of the statute and not on general principles of *res judicata. Merrill* v. *United States,* 152 F. 2d 74 (C.A. 2d). In the event, however, that this Court should disagree with the Government as to the effect of Section 322(c) on these actions, we submit that they are also barred

by the doctrine of *res judicata.*[4] The Supreme Court has discussed this doctrine with respect to tax cases in *Commissioner* v. *Sunnen,* 333 U.S. 591, 597-598, as follows:

> The general rule of *res judicata* applies to repetitious suits involving the same cause of action. It rests upon considerations of economy of judicial time and public policy favoring the establishment of certainty in legal relations. The rule provides that when a court of competent jurisdiction has entered a final judgment on the merits of a cause of action, the parties to the suit and their privies are thereafter bound "not only as to every matter which was offered and received to sustain or defeat the claim or demand, but as to any other admissible matter which might have been offered for that purpose." *Cromwell* v. *County of Sac,* 94 U.S. 351, 352. The judgment puts an end to the cause of action, which cannot again be brought into litigation between the parties upon any ground whatever, absent fraud or some other factor invalidating the judgment. * * *
>
> * * * *
>
> Income taxes are levied on an annual basis. Each year is the origin of a new liability and of a separate cause of action. Thus if a claim of liability or non-liability relating to a particular tax year is litigated, a judgment on the merits is *res judicata* as to any subsequent proceeding

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[4]/The fact that the prior suits were nominally against the Commissioner, and the present actions against the United States, does not vitiate the application of the doctrine. *Continental Petroleum Co.* v. *United States,* 87 F. 2d, 91 (C.A. 10th), certiorari denied, 300 U.S. 679; *Greenbaum* v. *United States,* 17 F. Supp 83 (C. Cls.); 10A Mertens, Law of Federal Income Taxation, Section 60.21.

> involving the same claim and the same tax year. But if the later proceeding is concerned with a similar or unlike claim relating to a different tax year, the prior judgment acts as a collateral estoppel only as to those matters in the second proceedings which were actually presented and determined in the first suit.

Taxpayers in the cases at bar are seeking to litigate their tax liability for the same year which they have previously litigated in proceedings before the Tax Court. *Schnitzer* v. *Commissioner,* 13 T.C. 43 affirmed *per curiam,* 183 F. 2d 70 (C.A. 9th), certiorari denied, 340 U.S. 911. But income tax liability for any one year is a single cause of action. *Commissioner* v. *Sunnen, supra; United States* v. *C. C. Clark, Inc.,* 159 F. 2d 489 (C.A. 5th), certiorari denied, 331 U.S. 818. There is no reason why taxpayers could not have raised the present issue in the prior proceedings before the Tax Court as an alternative argument to the effect that if the transfers of merchandise to Oregon Electric were held to be contributions to capital and not sales, then the taxes paid on the profit if any from those "sales" were erroneously paid. A correct tax deficiency or overpayment for the entire year could have been determined by the Tax Court, as it had jurisdiction to do. *United States ex rel Girard Co.* v. *Helvering,* 301 U.S. 540, 542. Taxpayers not having submitted to the Tax Court a claim which they might have, the decisions of that court became *res judicata. American Woolen Co.* v. *United States,* 18 F. Supp. 783, new trial denied, 21 F. Supp.

125, affirmed on rehearing, 21 F. Supp. 1021 (C. Cls.), certiorari denied, 304 U.S. 581.

Martin v. Brodrick, 177 F. 2d 886 (C.A. 10th), and *Magruder* v. *Safe Deposit & Trust Co.,* 159 F. 2d 913 (C.A. 4th), relied on by taxpayers below are not in point. Those cases involved attorneys' fees and expenses arising out of the litigation. Further, the courts are not in accord, even where such fees and expenses are involved in a second suit. *Cleveland* v. *Higgins,* 148 F. 2d 722 (C.A. 2d), certiorari denied, 326 U.S. 722; *Van Dyke* v. *Kuhl,* 171 F. 2d 187 (C.A. 7th).

III

IF TAXPAYERS ARE ENTITLED TO ANY RECOVERY, IT MUST BE COMPUTED BY DEDUCTING THE COST OF MERCHANDISE "SOLD" TO OREGON ELECTRIC FROM THE TOTAL COST OF GOODS SOLD BY ALASKA JUNK AS WELL AS BY DEDUCTING THE "GROSS SALES" PRICE OF MERCHANDISE TRANSFERRED TO OREGON ELECTRIC FROM THE TOTAL GROSS SALES OF ALASKA JUNK.

Taxpayers contend, and the District Court held, that they were entitled to reduce the gross sales shown on the partnership return by the sum of $347,341.62 which they assert was the total sales price of goods furnished by the partnership to Oregon Electric. Taxpayers also contend, and

the District Court held, that no corresponding adjustment should be made in the costs of goods "sold" to Oregon Electric. This, we submit, was error for any one of several reasons.

The finding of the Tax Court discussed under Point I, *supra,* that from October, 1941, the merchandise was furnished Oregon at cost, we submit is *res judicata* and determines for the purpose of these cases that no adjustment of the profit shown on the partnership return can be made.

In any event, it is a mere matter of mathematics that in determining the amount, if any, by which the partnership overstated its *net income* in its return it is necessary to take into consideration the costs of goods sold. This can be done (1) by taking the costs of the goods eliminated from gross sales from the actual sales price of the sales so eliminated, or (2) by deducting the full sales price from the total gross sales, and at the same time deducting from the total cost of goods sold the cost of the goods which have been eliminated from the total gross sales. A deduction of the total sales price alone would effect a reduction of the net income by that amount, and would in effect give to the taxpayers a loss of the costs of the merchandise. It is thus clear that in order to determine the partnership's net income the costs of such merchandise must be eliminated from the partnership's total costs of merchandise at the same time that the total "sales price" of the merchandise is eliminated from its total sales.

In fact, in their brief below taxpayers seem to so admit. Their contention was that income that is taxable is the net income determined from the operations for the entire year; that it was at the end of the year that economic gain or loss was to be determined based upon a computation of the entire year's experience; that to determine taxable income, all of the money expended for the purchases of merchandise during the year, and not only a portion thereof, must be deducted from gross sales; that the merchandise which the partnership delivered to Oregon Electric turned out to be worthless just like merchandise destroyed by deterioration. The argument, of course, is fallacious. The Tax Court and this Court have held that the merchandise was contributed to Oregon Electric by the individual partners. Certainly this is *res judicata.*

Further, taxpayers' position here, though stated in a different way, is the same as it was in the former actions—that the merchandise furnished to Oregon Electric turned out to be worthless. They make no attempt to show that any of the merchandise was destroyed, stolen, etc. But in any event, any loss which resulted from the contributions to Oregon Electric were not losses to the partnership, but were capital losses to the individuals (as stockholders of Oregon Electric (Tax Court R. 41)), limited by Section 117(d), of the Internal Revenue Code of 1939. That section allows losses to taxpayers, other than a corporation, from the sale or exchange of capital assets only to the extent of the gain from such sales or exchanges plus the net income of the tax-

payer or $1,000, whichever is smaller. No such loss is claimed here, and in so far as the record shows, the loss already has been taken.

CONCLUSION

The judgments of the District Court should be reversed, and no refunds whatsoever allowed to these taxpayers. But if the Court should hold that some refunds should be made, they should be figured in accordance with the method submitted by the Government in Point III of the Argument.

Respectfully submitted,

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